

John Engler, Governor

**THE MICHIGAN DEPARTMENT
OF ENVIRONMENTAL QUALITY**

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THE MICHIGAN MUNICIPAL BOND AUTHORITY

Janet Hunter-Moore, Executive Director

Under the Authority of Part 53, Clean Water Assistance, of the Natural Resources
and Environmental Protection Act, 1994 PA 451 and the Shared Credit Ratings Act, 1985 PA 227

Present the

**FISCAL YEAR 1998 ANNUAL REPORT
of the MICHIGAN STATE REVOLVING FUND**

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I. INTRODUCTION

This Fiscal Year (FY) 1998 Annual Report is submitted to the United States Environmental Protection Agency (EPA) in compliance with Sec. 602(b)(10) and Sec. 606(d) of the Federal Water Pollution Control Act, P.L.92-500, as amended. It covers the period from October 1, 1997 to September 30, 1998, highlighting the activities of Michigan's State Revolving Fund (SRF) loan program.

The Michigan Department of Environmental Quality (MDEQ) is the lead agency for this program. The Municipal Facilities Section (MFS) of the Environmental Assistance Division (EAD) continues to serve as the MDEQ's program administrators for the SRF.

The MDEQ and the Michigan Municipal Bond Authority (MMBA) jointly administer this program under the authority of Part 53, Clean Water Assistance, of the Natural Resources and Environmental Protection Act, 1994 PA 451, and 1985 PA 227, the Shared Credit Ratings Act, as amended. The state also conducts its SRF in a manner consistent with requirements established in the federal Water Pollution Control Act (P.L.92-500, as amended) and federal regulation.

We offer this comprehensive public report to detail the activities undertaken to reach the objectives set forth in the final FY1998 Intended Use Plan (IUP). This annual report is submitted to EPA and is available as a read-only file through the MFS Home Page found in the World Wide Web on Internet. The Internet address is <http://www.deq.state.mi.us/ead/mfs>.

II. CAPITALIZATION OF THE SRF

During FY1998, Michigan received a federal grant of \$57,899,853 on September 11, 1998. The state is required to provide a 20 percent match for each federal dollar contributed to capitalize the SRF. To match the FY1998 federal grant, Michigan provided \$11,579,971. The source of this match was derived from state general fund appropriations and state match bonds. In addition to the federal and state capital contributions, the SRF is also capitalized with principal and interest payments from earlier loans and from released funds from debt service reserve accounts. Please note that the federal capitalization grant accounts for only 40 percent of the total capital funds for Michigan's SRF. Thus, for FY1998, the total capitalization of the SRF was \$134,319,836. The breakdown is as follows:

Title VI Fund	\$57,899,853
Sec 205(m) Transfers	\$0
State Match	\$11,579,971
Principal Repayment	\$23,292,515
Interest Repayment	\$10,558,343
Investment Earnings	\$30,989,154

III. PROGRAM ISSUES

Binding commitments made during FY1998 were awarded with an interest rate of 2.25 percent. Repayments are amortized over 20 years with approximately level debt service. There were no loan guarantees or project refinancings provided during FY1998. All commitments were made to qualified Section 212 projects.

There were no commitments made to Section 319 non point source projects. We have continued working on the development of an assistance program targeting agricultural producers with non point source pollution prevention projects. Staff had worked to flesh out a proposal based on a linked deposit concept which could

be implemented on a trial basis. However, in meetings with Michigan bankers, it was clearly articulated that the bankers would not support a limited linked-loan program. It was too costly to participate in for the amount of business they would do.

We are now back to working with modifications to this concept that would be acceptable to loan participants and to the banking community. After passage of legislation to broaden the definition of a municipality, this program change could result in financing qualified agricultural projects through the SRF. The MDEQ will continue working to gain support for a viable non point source financing program during FY1999.

For FY1998, projects for qualified Section 212 uses were drawn from the FY1998 Project Priority List administered under provisions set forth in Part 53, Clean Water Assistance, of the Natural Resources and Environmental Protection Act, 1994 PA 451, and its accompanying administrative rules. A copy of this list was submitted to the EPA prior to the start of FY1998. Other interested parties may contact the MFS to receive a copy.

The MDEQ continues to promote the SRF in local community meetings, through continued dissemination of the SRF brochure and guidance documents, through The Loan Arranger, through the MFS website, and through participation in various public forums. Staff has at its disposal, a computerized presentation in Microsoft Powerpoint explaining the SRF. This presentation is targeted toward local community groups and can be tailored to a specific audience by adding, deleting, or editing the slides. The presentation is available in three separate media; slides, overheads, and a diskette and is also available for download through the EAD website.

IV. GOALS AND ACCOMPLISHMENTS

A. Short-Term Goals and Accomplishments

Michigan's IUP described five short-term goals to be implemented during FY1998. They were:

1. **To continue on-going revisions to the SRF Procedures Manual. This is a continual process involving staff and management effort to review and redraft chapters to reflect changes in operational procedures of managing the SRF. This will result in improved efficiency and effectiveness of the program.**

Changes to the SRF Application were completed and the new SRF Application was used this year. Part 2 and 3 of the application received minor changes, however, Part 1 underwent major revisions. Based upon survey results and customer input, the financial information in Part 1 was consolidated from 16 pages to 10 pages. The result is a tighter focus on the financial documentation required for submittal.

The customer feedback from these revisions has been very positive with comments ranging from "less burdensome" and "more concise" to "more user friendly." The MFS believes in the importance of a program that is responsive to its SRF customer needs and will continue to revise program documents as the SRF continues to evolve and mature.

2. **Implement a new Drinking Water Revolving Fund (DWRF) as a companion program to the SRF in Michigan.**

Governor John Engler signed 1997 PA 26 into law on June 17, 1997. This amended 1994 PA 451, the Natural Resources and Environmental Protection Act, to create Part 54, Safe Drinking Water Assistance. Through Part 54, the DWRF became the companion financing program of

the SRF for water pollution control. DWRF loans were first made available in the third quarter of FY1998.

In order to facilitate the implementation of the DWRF program and maintain the existing level of performance in the SRF program, four new MFS staff members were hired to increase project management capacity. Extensive training for new and transferring employees took place during the weeks of April 6-17, with training on specific matters continuing throughout the year.

As a result of the increased staff size and the dedication of existing staff, Michigan was recognized at the 1998 Council of Infrastructure Financing Authorities (CIFA) SRF National Workshop as one of the top five states in the country for DWRF loan awards during FY1998. Michigan awarded \$53,775,000 for 24 projects. In FY1999, Michigan anticipates funding 19 projects with over \$47,000,000.

3. Establish a Small Community Hardship Assistance Program and a viable non point source Agricultural Revolving Fund for use during FY1999 and beyond.

Michigan has continued to look for opportunities to provide assistance to small communities in hardship situations. One of the stumbling blocks to implementation of any type of hardship assistance program to accommodate the available federal money is that most communities in Michigan are already sewered. The existing federal funds are targeted towards unsewered communities and are too restrictive for Michigan's existing situation. Michigan will continue to explore possibilities during FY1999 to assist small communities experiencing economic difficulties.

The Clean Michigan Initiative (CMI) was placed on the ballot in November, 1998. This initiative, a \$675 million plan for environmental and economic development, was approved by the citizens of Michigan. A number of objectives have been identified for distribution of these funds and include protection and enhancement of Michigan's lakes, rivers and streams; environmental clean up; and pollution prevention. The specific programs which the initiative will fund have yet to be determined. However, the discussions which have occurred regarding the Agricultural Pollution Prevention Program are being raised again as part of the CMI. The implementation of the Agricultural Revolving Fund has been delayed until initial program funding issues have been addressed.

4. To identify and establish a technical assistance program for municipal revenue system development, focused on pollution prevention through outreach.

The Technical Support Unit staff of the MFS have participated in several seminars and have made on-site visits around the state to discuss revenue systems with municipalities and consultants. Visits included a workshop on replacement for plant operators in Huron County, a user charge system discussion with South Huron Valley municipalities, and on-site meetings with Escanaba, Manistee, Sault Ste. Marie, Mt. Clemens, and Kent City. The shift from an enforcement mentality to one of assistance is a gradual transition. For many municipalities, our office is still looked on as an enforcement agency. The MFS will continue to provide technical assistance to municipalities and take advantage of expanding opportunities in order to reinforce the customer service aspects of our program.

The unit has also begun working on revisions to the user charge system review and approval process. The first effort is directed at the submittal process and providing applicants with more

consistency between the DWRP and SRF programs and a greater amount of flexibility in program deadlines. The second effort is directed at developing new guidelines for the user charge system submittal itself.

5. To work with the EPA and the Association of State and Interstate Water Pollution Control Administrators (ASIWPCA) to promote reauthorization of the Federal Clean Water Act

During the FY1998 annual meeting of the of ASIWPCA, Michigan was once again appointed vice-chair of the Municipal Facilities Task Force. The ASIWPCA believes that greater focus should again be placed on issues relating to municipal infrastructure financing. Given Michigan's past leadership, the ASIWPCA board of directors asked Tom Kamppinen, Chief of the MFS, to serve in this capacity.

In addition, the CIFA asked Michigan to participate in a workgroup designed to seek more active input from state and local water administrators regarding the SRF programs.

6. To fund those projects identified in the IUP, enabling them to proceed with construction of facilities included in their adopted project plan.

In each of the first and second quarters, one project was funded at \$525,000 and \$6,645,000, respectively. In the third quarter, seven projects totaling \$32,360,000 were funded, while in the fourth quarter of FY1998, nine projects received binding commitments equaling \$87,395,000. For the full fiscal year, the MDEQ and the MMBA committed \$126,925,000 to 18 projects, bringing the total commitments made from inception of the SRF to \$833.8M. Closings have taken place on 148 projects during the life of the SRF to date.

B. Long-Term Goals and Accomplishments

Michigan's IUP also included six long-term goals that would be addressed by the SRF. They were:

1. To achieve and maintain statewide compliance with all applicable State and Federal laws, rules, and standards.

The SRF is a major inducement for local municipalities to cooperate and voluntarily seek to achieve compliance with state and federal laws and water quality standards.

The MDEQ maintains a core belief that achievement of pollution prevention is far more effective if potential projects are examined to ensure compliance with water quality standards, while also meeting criteria to establish the solution as the cost-effective alternative in order to protect the viability of the SRF.

In past years, Michigan's SRF program has provided substantial assistance in funding towards combined sewer overflow (CSO) abatement efforts. The state has funded sizable projects in Grand Rapids, Lansing, and Saginaw. Most recently the state has funded projects for smaller municipalities such as Manistee and Sault Ste Marie. While over the life of the SRF, **48 cents of every dollar** loaned has been used for correction of CSO problems, there is still work to finish. The SRF will continue to fund necessary CSO projects as they arise and anticipates Phase II Rouge River projects, as well as those from the city of Detroit, over the next few years.

2. To protect the public health and environmental quality of our state.

Inherent within the SRF program is our resolve to first protect the public's health and welfare. Our priority system is structured to give greatest weight to problems which most impact the health of Michigan's citizens and the environmental integrity of our state.

The state's Project Priority List establishes the list of fundable projects for each fiscal year. Projects are ranked using a number of criteria including outstanding enforcement action against proposed applicants. Michigan places a high priority on resolving those situations where enforcement action is involved and, accordingly, any enforcement action against a community plays a crucial role in establishing that community's position in the fundable range. Many of the projects at the top of the fundable range are involved in an enforcement action of some type.

Of the 148 projects funded, 89 (or 60 percent) of the projects have addressed critical public health or environmental quality concerns. These 89 projects represent over \$533,255,000 in funds dedicated to substantially improving the quality of our state's waterways.

3. To develop an Agricultural Revolving Fund for private producers to provide easier access integrating Section 319 non point source pollution projects into the mainstream of the SRF.

See number 3 under Short-Term Goals.

4. To further integrate principles of watershed management and water quality restoration within urban, as well as outstate, areas.

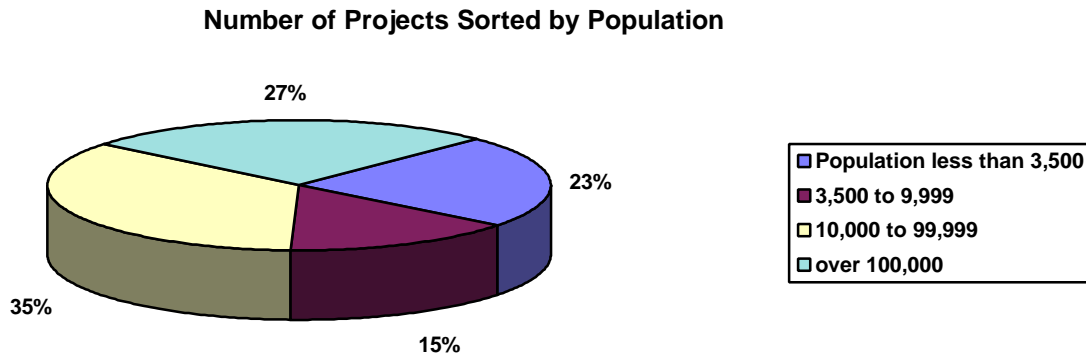
One of the MDEQ's major initiatives is the redevelopment of urban brownfield areas in hopes of preventing the continued degradation of open farm lands. Whenever an urban project has scored high enough in priority, the SRF has sought to provide financial assistance to improve the water quality of the project area.

We have already sought to incorporate the watershed sensitivity into our project management. A good example continues to be the commitment to the city of Lansing for its CSO strategy, which reduces pollutant loadings in the Grand River watershed. Our continuing efforts to work with communities in the Rouge River watershed in addressing their needs also reflects our commitment to watershed management.

While the SRF has funded substantial projects in outstate Michigan, it has contributed substantial assistance to urban communities such as Lansing, Grand Rapids, Detroit, Wayne County, Saginaw, and communities tributary to Lake St. Clair, to address major needs within each. Of the total SRF loan dollars distributed to date, 38 percent has been awarded to projects with service areas in excess of 100,000 population.

The accompanying charts document the progress made since the inception of the program. Michigan's commitment to small communities remains equally strong. Of the 18 projects funded this year, 10 projects representing \$33,550,000 in construction costs were for communities with populations less than 10,000. Over the life of the SRF, a total of 57 loans, or 38 percent of loans made, were issued to communities with population less than 10,000. In dollar volume, almost \$157,575,000, or 18 percent of total binding commitments went to these smaller communities. To date, the numerical distribution of SRF loans is as follows:

Population less than 3,500	\$ 84,485,000
3,500 to 9,999	\$ 73,090,000
10,000 to 99,999	\$365,530,000
over 100,000	<u>\$310,700,000</u>
TOTAL LOANS	\$833,805,000



- 5. To secure Michigan's full share of federal funding available under Title VI and to expeditiously obligate these moneys, along with state contributions, for the construction of water pollution control activities that meet state and federal requirements.**

The SRF has applied for and received all available capitalization grants through FY1998's federal appropriation. These funds are being committed to local units of government in an expeditious manner. In addition, the released moneys generated from satisfaction of the debt service default tolerances have also been made available for loan commitment within the fiscal year following release. Michigan's reliance on federal capitalization grants has now diminished to the point that the federal contribution to the SRF represents only 25 percent of the total amount available.

- 6. To establish an effective program of community environmental education, outreach, and involvement within watersheds.**

The MFS continues to expand the amount of information available through its homepage and makes available all pertinent documents for public viewing. In addition, many of the documents are being converted into the PDF format for easier downloading by interested internet users. The MFS plans to convert all documents on its website to the PDF format in 1999 to provide for a more consistent viewing presentation. Our SRF Database is available over the Internet to allow other states to review what we have accomplished in Michigan.

The website also includes the Student Information Kit and the Sharing Michigan's Watershed information. A link to the MDEQ's Surface Water Quality Division watershed site is also provided.

The MFS has redesigned its Digester newsletter to include DWRF program issues and renamed the publication The Loan Arranger. It now circulates to a combined readership of approximately 1700 readers interested in water supply and water treatment issues.

7. **To develop strategies within the SRF to help smaller, hardship communities meet water quality standards.**

See number 3 under Short-Term Goals.

V. DETAILS OF ACCOMPLISHMENTS

A. Fund Financial Status

1. **Binding Commitments:** The SRF made 18 additional binding commitments to Section 212 projects during the fiscal year. The state's commitments are made in the form of Orders of Approval issued by the Chief of the EAD on behalf of the MDEQ.

Chart 1 (Funded SRF Projects to Date) provides a complete, chronological list of all projects assisted by the SRF to date. Cumulative loan amounts and number of projects funded in each fiscal year are included.

During FY1998, \$126,925,000 was committed for project assistance. The total cumulative binding commitments to communities equals \$833,805,000 as of September 30, 1998.

These amounts are reflected on Chart 2 and demonstrate how Michigan's SRF satisfies Sec. 602(b)(3) of the federal Clean Water Act. This chart documents Michigan's progress in offering binding commitments to exceed the required 120 percent of federal Automated Clearinghouse (ACH) increases within one year. Through the end of FY1998, Michigan was required to commit \$680,447,411 in loans. In fact, \$833,805,000 has been identified as binding commitments apart from the administrative expenses incurred and paid to date. If we include the actual administrative expenses incurred by the MDEQ and the MMBA to date, which is counted by the EPA toward binding commitment, the total is increased to \$850,059,607.

2. **Capitalization Grants:** The Michigan Water Pollution Control Revolving Loan Fund was awarded a capitalization grant of \$57,899,853 from FY1998 federal funds. This amount was matched by the state with an \$11,579,971 contribution from general funds and state match bonds. Loans were awarded from these funds, the remaining uncommitted balances from earlier awards, and from investment earnings and repayments from earlier loans.

Payments on the capitalization grants increased the funds available through the ACH process. The increase in ACH payments made by the EPA during the fiscal year totaled \$55,655,127 which was the remaining balance from the FY1996 capitalization grant. All other federal capitalization grants have been increased to the full amount of their awards as of the end of FY1998. Chart 2 also presents the federal payments to Michigan, by quarter, for each of the awarded federal grants. It summarizes activities from FY1989-1995 and then provides detail for the three most recent years.

3. **Other Revenue:** In addition to the capital provided by the EPA and the state, principal repayments of \$23,292,515 and interest repayments of \$10,558,343 were made to the SRF by local borrowers of earlier fiscal year funds. Other sources of investment income, totaling \$30,989,154, were also generated from fund holdings and will be identified in the MMBA financial reports. The SRF also recovered \$5,041,940 from 23 projects that were

administratively completed during FY1998. This brings total recoveries to \$13,021,790 over the life of the SRF. These recoveries represent project costs which are less than the budgeted amounts committed at the time the MDEQ Order of Approval was issued.

4. Disbursements: Additional disbursements of \$112,564,394 were made during FY1998, bringing the total during the program's life to \$647,235,537. This means Michigan's SRF has dispersed 78 percent of the project commitments to date. This amount includes administrative expenses accrued to the MMBA during the fiscal year in the amount of \$151,283. Expenses accrued to the MDEQ for the same period of time totaled \$3,594,847. (For the sake of clarity, it should be noted that expenses are accrued for the fiscal year and may not be fully disbursed in cash prior to the end of the year.) These amounts are identified in Chart 5, Sources/Uses of SRF Funds.
5. Audit Report: An audit of MMBA's financial records for the SRF will be forwarded upon completion in the near future. Unaudited financial records will be sent under separate cover from the MMBA.

The last audit concluded by Plant Moran during FY1998 found that the SRF program reporting procedures were in compliance with Generally Accepted Accounting Principles, and also encompassed Generally Accepted Governmental Accounting Standards. The audit supported findings of the 1997 Annual Report submitted December 27, 1997.

We believe these financial statements reflect the condition of Michigan's SRF and underscore the sound management necessary to ensure the health of the fund in relation to its goals and objectives. This state has fulfilled requirements found at 40 CFR 3135(h) by establishing fiscal controls and accounting procedures to assure proper accounting for payments received by the SRF, disbursements made by the SRF, and SRF balances.

The Auditor General of the State also conducted an audit of MDEQ, which included the SRF. The audit findings were not yet complete as of the end of FY1998.

6. Credit Risk of the SRF: Michigan undertakes an exhaustive review of each applicant's credit-worthiness. This review examines the financial health of the community and its primary commercial and industrial base. The resulting approval of each applicant provides a sound basis for awarding assistance to only those communities possessing the ability to repay the loan.

No assistance is offered to any community that is unable to demonstrate an investment grade rating. If a community cannot demonstrate a minimum investment grade rating, we expect them to seek credit enhancement or finance through another governmental agency (such as the county). This must be done in order to secure their credit position before the Order of Approval can be written. Michigan's SRF has never suffered a payment default from any municipality.

B. Assistance Activity

Loan assistance through the MMBA was awarded to each of the municipalities that received an Order of Approval from the MDEQ. These are included in Chart 1. No other qualified uses of the funds were made other than project and administrative funding.

C. Provisions of the Operating Agreement/Conditions of the Grant

The state of Michigan agreed to a number of conditions in the Operating and/or Capitalization Grant Agreement. These conditions are described below:

1. Provide a State Match: The Michigan Legislature appropriated the amount necessary for the 20 percent FY1998 state match. In addition, Michigan has sold state match revenue bonds to make up the balance not appropriated. In the past, the match was held in a state common cash fund administered by the Michigan Department of Treasury. For FY1998, however, the amount from the state General Fund was deposited in full to the SRF accounts. The MMBA now administers the match accounts as part of their overall financial management.
2. Binding Commitments: The state entered into 18 binding commitments to provide assistance from the SRF to local municipalities. By the act of offering these commitments during FY1998, Michigan continues to exceed the requirement for award of 120 percent of the payment amount within one year. Documentation of performance is shown in Chart 2.

Additionally, we account for \$16,267,546 in actual administrative expenses, which are also applied against the state's binding commitment requirement. The EPA allows the State to account for the full 4 percent of the federal capitalization grants to be applied against binding commitments at the time of each grant award. Michigan has chosen to account only for actual administrative expenses against binding commitments for programmatic reasons.

3. Expeditious and Timely Expenditure of Available Funds: The EPA annually reviews the reimbursement process used by the MDEQ and the MMBA to ensure that payments to municipalities are made in a timely and expeditious manner. In most instances, a wire transfer occurs within ten days of receipt of a request for reimbursement from the local unit of government. The EPA on-site visits have affirmed Michigan's sustained ability to turn payment requests around quickly. The local communities and the contractors know that we will expeditiously handle this important task, ensuring no delays in the flow of funds to the project. Documents upon which this assessment is based are available for inspection at the MDEQ and the MMBA offices, and are included in the SRF database.

The federal share is provided through the federal ACH. State funds are drawn simultaneously with the federal funds during this time. The state portion is drawn through the treasury inter-accounting system. The draw method used in Michigan satisfies our state requirements to provide a state match prior to, or at the time of, the federal draw on the ACH system.

To date, Michigan's SRF has committed \$883,805,000 in project loans. Administrative expenses, which EPA also counts toward binding commitments equal \$24,997,575, assuming 4 percent of all federal capitalization grants to date. Accounting for the reserve requirement for bonds sold, Michigan is ensuring expeditious commitment of the available money in the SRF to local municipal projects.

4. Amendments to the IUP: The final IUP and Project Priority List for FY1998 were submitted to the EPA in November, 1997.

5. Minority and Women's Business Enterprises: In order to meet federal initiatives, the state of Michigan agreed to an overall fair-share objective for FY1998 of 4 percent for Minority Business Enterprise (MBE) and 4 percent for Women's Business Enterprise (WBE). In its attempt to meet this objective, the state advised all potential applicants for SRF loans of this commitment. In addition, the state included a reporting requirement as a special condition in all supplemental agreements executed between the loan recipient, the MDEQ, and the MMBA. As part of the state's continuing effort to meet the MBE/WBE objective, presentations are made at the pre-bid meetings to explain the federal requirements to potential contractors, subcontractors, and suppliers.

Compliance with the loanee's reporting requirements has shown that the state of Michigan has exceeded its MBE objective for FY1998 by reaching an actual participation of 5.2 percent for MBEs. The goal for WBE participation fell short, finishing FY1998 with 3.4 percent for WBEs. These figures were reported on October 23, 1998 to Ms. Karen Jurgensen, Office of Financial Services, MDEQ, as part of the state's required submission during the fourth quarter of FY1998.

6. Other Federal Authorities: The state of Michigan requires each municipality to comply with all applicable federal cross-cutting authorities and stipulates that the authorized representative so certify in the application. The Application for Assistance sets forth municipal requirements for compliance with federal cross-cutters.

We seek up-front coordination by involving a wide range of agencies in the Finding of No Significant Impact (FNSI) process during drafting of the Environmental Assessment. These federal, state, and local agencies are given the chance to add input to the project and comment on any cross-cutting issues.

Environmental cross-cutters are typically addressed during review and approval of a project plan. Activities conducted by MDEQ staff are presented in the Project Planning/ Environmental Assessment chapter of our SRF procedures manual.

Cross-cutting issues relating to social legislation are dealt with prior to the loan award through applicant certifications mentioned earlier and through follow-up reporting, such as in the case of MBE/WBE requirements.

Our staff procedures manual outlines the appropriate response in the event cross-cutting issues arise. When warranted, we coordinate contacts with appropriate agencies. If necessary, the state will seek assistance from the EPA for help with non-agency federal offices.

7. State Environmental Review Process: The 18 communities receiving assistance during FY1998 were reviewed and approved using the state's environmental review procedures. It was determined that no Environmental Impact Statements were necessary, instead an Environmental Assessment was prepared and a FNSI was issued for each project.
8. Consistency with Planning: No project plan in the state of Michigan can be approved without sign-off from the appropriate 208 planning agency, which documents the submittal is consistent with regional planning. Assurance of this review is inherent within each and every plan we approve.

Section 205(j) and 303(e) requirements are administered separately from the SRF by various sections of the MDEQ Surface Water Quality Division. Grants have been made to several local and regional entities to carry out water quality management planning. Sec. 303(e) requirements are satisfied via our state permitting process. In order to continue Michigan's delegated permit writing program, the state must comply with Section 303(e). Prior to receiving the first capitalization grant, this office verified the existence of an approved planning process. The EPA's continued recognition of our delegation is proof that we remain in compliance.

9. Cash Disbursements: Procedures are executed in conjunction with the MMBA. The MDEQ receives requests for disbursements from the local municipalities. We review them for content and accuracy and then transmit them simultaneously to the MMBA and the MDEQ's Office of Financial Services. The respective offices will process a request for a state match transfer into the SRF and process a request to draw on the federal ACH system in accordance with 40 CFR 35.3135(b)(1). Once in the SRF account, the MMBA processes a wire transfer of funds to the local municipality.
10. Administration of the SRF: The MDEQ has agreed to administer the SRF in accordance with its application, IUP and the Operating Agreement. In doing so, certain administrative procedures are implicit. The operation of the fund is bound by the following provisions:
 - agreement to accept payments
 - state laws, rules, and procedures
 - state accounting and auditing procedures
 - recipient accounting and auditing procedures
 - use of the ACH federal payment system
 - repayment
 - annual audit requirements
 - annual report
 - annual review

To the extent of any conflict amongst these documents, the MDEQ further agreed that terms of the Grant Agreement will prevail.

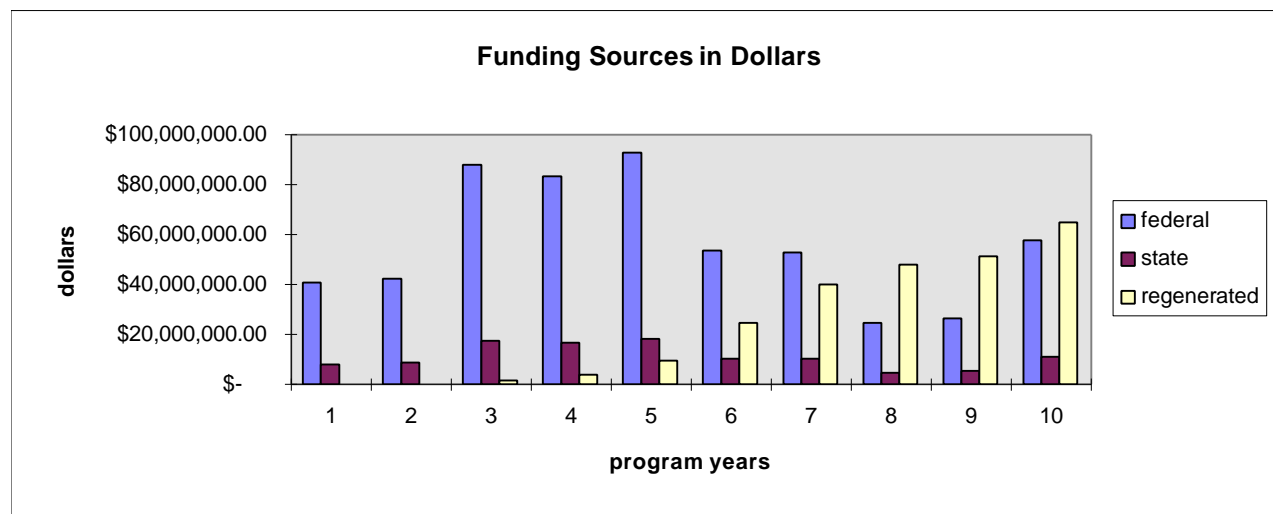
11. Automated Clearinghouse: Michigan has agreed to accept payment from the EPA through the ACH system and has abided by cash draw rules.
12. Legal Certifications: The state of Michigan has provided all necessary certifications from the state Attorney General's office, which attest to its ability to implement the SRF and bind itself to the terms of the Capitalization Grant Agreement. The certification for the FY1998 capitalization grant was dated June 12, 1998.
13. Cash Draw Schedules: The cash draw figures set forth in Chart 6, Project Disbursements, reflect chronological disbursements made to each project during the fiscal year. In its final IUP for FY1998, Michigan had requested a cash draw in the first quarter of \$18.47M; \$15M in the second quarter; \$15M in the third; and \$10M in the fourth quarter. Charts 2 and 5 both reflect the actual ACH activity during the current fiscal year, as well as show the historical summary of all draws to date.

VI. SIGNIFICANT PROJECT ACCOMPLISHMENTS OF THE SRF

To date, Michigan's SRF has awarded \$883.8M in loans. We have awarded 83 percent of the funds available, with the balance held on reserve against bond default. Interest repayments from earlier awards are being held for possible repayment of state revenue match bonds for future issues. Principal payments from these loans and investment earnings have been building and will be used to supplement declining federal capital contributions. This strategy allows us to better maintain program expectations with the municipal, consulting, and contractor stakeholders.

Of the total amount loaned during FY1998, \$57,899,853 came from the EPA Capitalization Grant, \$11,579,971 came from the state match, \$23,292,515 and \$10,558,343 came from principal and interest respectively from outstanding loans, and \$30,989,154 came from investment earnings. Funds generated from the SRF program itself provided \$57,445,176 or 45 percent of the \$126,925,000 loaned out during FY1998.

Over the lifetime of the Michigan SRF program, the dependence on federal dollars for capital funds has diminished to a point where the dollars capitalized through principal, interest, and investment exceeds those dollars received from the EPA Capitalization Grant. This shift from federal funds to SRF generated funds for financing SRF projects is a testament to the philosophy of the revolving fund concept. Michigan, through its efforts to maximize initial funding opportunities and in turn, loan those funds out, has created a viable revolving fund mechanism. The graph below shows how the infusion of funds generated from the SRF has increased over the life of the program to a point where they exceed federal Capitalization Grant dollars.



The interest rate for projects funded during the first five years was 2 percent. For 1995 projects and beyond, the rate increased to 2.25 percent.

The SRF is proving to be much more efficient in administratively completing projects than its predecessor, the Construction Grants Program. A list of all projects administratively completed through September 30, 1998 is included as Chart 8. Staff administratively completed 23 projects during FY1998, bringing the total completed to 79. This total represents 53 percent of all loans awarded to date.

Chart 7 - Project Initiation of Operation (I/O) Dates, demonstrates the projects that have actually commenced operation during FY1998.

To date, Michigan's SRF has gone to the market for seven issues. Bonds totaling \$91,110,100 were sold in 1992. In 1993, \$102,220,000 were sold. The third issue in early 1995 totaled \$87,280,000, while the fourth issue was sold for \$86,290,000 in May, 1996. A fifth issue was sold for \$132,500,000 in June, 1997. On July 15, 1998 a sixth issue was sold for \$151,165,000. These bonds are used to provide disbursement proceeds for project draws and are timed to cover a period running from 12 to 15 months at a time. In addition to the regular bond sales, a refinancing of \$86,750,000 was conducted in August, 1996 to defease series 1992A and 1994 bonds.

In selling the bond issue for the SRF and the DWRF in 1998, the State sought bond ratings from both Moody's Investor Services and Standard & Poors. The rating agencies increased the ratings on SRF bonds to Aaa & AA1, respectively, showing a high level of confidence in the financial integrity and administrative capability of the MDEQ and the MMBA.

VII. CONCLUSIONS

Michigan's SRF program has matured into a well run, well received financing program. The state has been able to deliver its available funds in a manner that emphasizes consistency of environmental review, financial capability standards, as well as delivery of reimbursement for project costs. There have been 148 projects funded to date, delivering over \$833 million in loans. The moneys which capitalize the SRF are now derived predominately from repayments and earnings on investments. The original intention of developing the SRF as a revolving, self-supporting fund is now being realized. Although the annual federal contribution is still present, it accounted for less than one-third of the total capital pool this year.

Staff of the Municipal Facilities Section have continued to effectively manage the SRF program for water pollution control, while investing significant time initiating a successful DWRF. Additional staff have been trained and integrated into the existing staff. The MFS staff are responsible for both DWRF and SRF projects, and work diligently to ensure that projects in both programs receive full attention. The MFS remains committed to customer service and through shared experiences and customer feedback, revisions and improvements to both programs are implemented on a periodic basis. We believe that the staff commitment to each program is the principal reason that Michigan's revolving fund programs will continue into the future with high visibility and success.